No. 17038

United States
COURT OF APPEALS
for the Ninth Circuit

EQUITABLE LIFE AND CASUALTY INSURANCE CO.,

Appellant,

vs.

VIRGIL N. LEE,

Appellee.

BRIEF OF APPELLEE, VIRGIL N. LEE

Appeal from the United States District Court for the District of Oregon.

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The statement of the case and the statement of facts as set forth in the brief of the appellant are not such as need any further statement or clarification on the part of the appellee.

SUMMARY OF ARGUMENT AND STATEMENT OF JURISDICTION

(1) The appellant contends that this action was brought to rescind the contract of insurance (Ex. 1).

However, the only matters in any of the pleadings that raised the issue of rescission are to be found in paragraphs 6, 7, 8, 9 (R. 15, 16) of defendant's contentions in the amended pretrial order. The complaint does not set out any matter necessary to invoke the intervention of a court of equity. The complaint and all of the contentions of the plaintiff set forth in the amended pretrial order sound in tort and a tort case can not be converted into one of rescission by the defendant though he may raise equitable defenses to a law action. The case was presented and tried as a tort action, with the equitable defenses rejected by the trial court (R. 164).

In order to invoke the aid of a court of equity it is necessary to plead and establish by proof the fact that the plaintiff *has no plain, speedy and adequate remedy at law*. No such plea was made because a remedy at law was available. Likewise, punitive damages are never asked for in an equity proceeding, and are a fundamental part of both the complaint and the pretrial order. Consequently the rescission theory of the appellant is not tenable. Likewise, its challenge to the jurisdiction of the court on that ground fails, since the amount prayed for in the complaint exceeded the jurisdictional requirements to bring the case within the purview of federal jurisdiction, and unless the court can say that there is no possibility of recovery of the amount prayed for to give the court jurisdiction, then jurisdiction in the federal court lies.

(2) The theory of the case was never changed at any time from a tort theory, and the trial was conducted on that basis.

(3) There is ample evidence to support the findings of fact and conclusions of law.

(4) Corporations under Oregon law are liable for punitive damages.

(5) Since the plaintiff was proceeding in an action at law he is not required to act with the speed demanded in a rescission under an equity theory.

(6) In an action for damages on a tort theory, the return of dividends was not required.

(7) The plaintiff in order to waive any of his rights must act with full knowledge of not only his rights but what he is waiving, and he had neither the knowledge of his rights and by his action has not waived his right to bring an action for damages.

(8) Plaintiff did not attempt to rescind and was not required to act promptly.

(9) Plaintiff relied upon the representations of the selling agent and the general agent of the defendant in entering into the insurance contract with the defendant.

ARGUMENT

(1) This action as evidenced by the pleadings, amended pretrial order and the trial of the case, was for damages suffered by the plaintiff having been induced to purchase an insurance contract through fraudulent misrepresentations of the agents of the defendant.

The case was tried on a tort theory; and under Oregon law, punitive damages are available in a proper case.

Since the amount pleaded for was in excess of the jurisdictional requirement, jurisdiction lies in the federal court as the amount in controversy exceeded the limit of $10,000.00.

The trial court rejected the defense of rescission asserted by the appellant (R. 164), and properly held that the United States District Court for the District of Oregon had jurisdiction of the parties and of the subject matter and decided the case on the theory presented by the appellee. The fact that the amount recovered in general and punitive damages by the appellee was less than the jurisdictional amount is not determinative of jurisdiction.

In the case of *Firemans Fund Ins. Co.* v. *Railway Express Agency,* 253 F.2d 780, the court says, at page 783:

> "This court also made similar rulings. In Calhoun v. Kentucky-West Virginia Gas Co., 6th Cir., 166 F. 2nd 530, we pointed out that jurisdiction must be distinguished from the merits and that unless the claim set forth in the pleading involving the necessary jurisdictional amount is plainly unsubstantial, either because obviously without merit, or because its unsoundness results so clearly from court decisions as to leave no room for the inference that the questions sought to be raised can be the subject of controversy, a case is presented within the federal jurisdiction regardless of the fact that a final judgment on the merits fails to establish the necessary jurisdictional amount."

It is true that in this case the court applied the out-of-pocket rule with respect to actual damages. Nonetheless, that ruling does not automatically convert the

case into one of rescission, nor oust the federal district court from jurisdiction.

(2) The plaintiff did not change his theory of the case at any time.

Since the appellant had raised the issue of rescission and it was still a matter for the determination of the court as to whether the court would accept the theory of the appellee or that of the appellant, it was incumbent upon the appellee to inform the court that he was prepared to return the last dividend check (Plf's Ex. 8) for $100.00. That did not change the theory of the plaintiff's case in any degree.

(3) The findings of fact and conclusions of law are supported by the evidence.

The court found that there was fraud in the sale of the policy of insurance involved (R. 136, 137, 161), and further found that there was no waiver on the part of the appellee by his course of action (R. 20, 142).

The case of *Herman* v. *Mutual Life Insurance Company of New York,* 108 F.2d 678, 127 A.L.R. 1464, was a case in which rescission was sought, as contrasted to the case at bar where damages were sought. In the Herman case the plaintiff retained his policy of insurance and accepted the benefits therefrom for a period of approximately six years, and then sought to rescind. Basically the court there held that if one seeks to rescind on the basis of fraud, he must act promptly after learning of the fraud or he is not entitled to rescind. The Herman case has no application, by reason of the

fact that rescission is not the relief sought by the appellee.

The case of *Sheppard* v. *Blitz,* 177 Or. 501, 163 P.2d 519, is ample authority that one seeking damages, as contrasted to rescission, by reason of fraud, does not need to act with the same dispatch as he would do if he were seeking to rescind.

In *Sheppard* v. *Blitz, supra,* the plaintiff instituted an action against Blitz individually and as trustee in February of 1938. In March of 1940 A. I. Blitz died and his widow, who was executrix of his estate, was substituted in his place individually. No substitution was made for A. I. Blitz as trustee. The plaintiff sought to rescind a contract previously entered into with A. I. Blitz individually and as trustee, on the ground of fraudulent misrepresentation. A decree was entered by the trial court in accordance with the prayer of the complaint. The decision of the trial court was reversed by the Supreme Court of the State of Oregon on June 9th, 1942, 168 Or. 691, 120 P.2d 509, on the ground that there was a defect of parties defendant, and returned to the trial court for further proceedings. Pursuant to an order entered by the trial court the plaintiff was permitted to amend his complaint and proceed against the estate of A. I. Blitz individually in a tort action seeking damages for fraudulent misrepresentation. Judgment was entered in the trial court in behalf of the plaintiff, and an appeal was taken by the defendant. The case was decided by the Supreme Court of Oregon November 14th, 1945, more than eight years after the

original complaint was filed, and sustained the trial court on the question of damages.

The Supreme Court of Oregon reviewed the cases bearing on the subject, and found that the plaintiff could bring his action for fraud on a tort theory even though he had previously proceeded to trial on an equity theory of rescission.

The case of *Sheppard* v. *Blitz, supra,* is authority for the fact that one does not have to act with the same dispatch where damages for fraud are sought, as he must do where rescission is the remedy.

There is no admission on the part of the appellee or any evidence in the record that he did not act with promptness upon learning all of the facts with respect to the contract he had been induced to enter into, by reason of the fraudulent misrepresentations. He affirmed his contract, as was his right to do, and sought his remedy in damages.

As the case of *Scott* v. *Walton,* 32 Or. 460, 52 P 180, sets out:

> "A party who has been induced to enter into a contract by fraud, has upon his discovery, an election of remedies. He may either affirm the contract and sue for damages, or disaffirm it, and be reinstated in the position he was before it was consummated. These remedies, however, are not concurrent, but wholly inconsistent. The adoption of one is the exclusion of the other."

The opinion continues:

> "If he desires to rescind, he must act promptly and return or offer to return which he has received under the contract. He can not retain the fruits of

> the contract awaiting future developments to determine whether it would be more profitable for his to affirm or disaffirm. Any delay on his part, and especially his remaining in possession of the property received by him under the contract, and dealing with it as his own, will be evidence of his intention to abide by the contract."

The case of *Grange* v. *Penn Mutual Life Insurance Company,* 235 Pa. 320, 321, 84 Atl. 392, 396, and the other two cases cited by appellant deal with a matter of rescission where the plaintiff in each of the cases sought relief long after learning of the fraud, and retaining the benefits of the policy involved, which is not the case here. They deal with rescission, and this case deals with damages, so are certainly not authority for the decision of this court.

Plaintiff's Exhibit 4, "You Have Been Nominated" and Plaintiff's Exhibit 5, "Hidden Ways to Wealth" are certainly vivid examples of literature distributed by the agents of the company that made possible the perpetration of fraud as was practised in this case. Plaintiff's Exhibit 5, "Hidden Ways to Wealth" was approved by the company (R. 128) according to the testimony of Mr. Raymond R. Ross, assistant general manager, superintendent of agents for Equitable Life and Casualty Insurance Co., of Salt Lake, the defendant (R. 115, 116). The testimony of Dr. Lee with respect to the statements made to him relating to dividends that the company would pay on a policy of this type, by the agents of the company including the general agent, Mr. Reklau (R. 41, 42, 43, 44, 46, 47) certainly support the court's finding that the policy of insurance in question

(Plf's Ex. 1) was sold by fraudulent misrepresentations, even if we disregard Plaintiff's Exhibit 6 which Dr. Lee testified was shown to him and discussed with him by Mr. Reklau, the general agent of the company. Dr. Lee testified (R. 50) that he relied upon the statements made by the agents, including the general agent, in the purchase. Consequently there is ample evidence to support the finding that the policy was sold and purchased by reason of the fraudulent misrepresentations of the defendant's agent and that the defendant knew of some of the material being used to perpetrate the fraud, in having approved for use Plaintiff's Exhibit 5. Nowhere does the defendant deny that they disapproved the use of any of the other material, such as Plaintiff's Exhibits 5, 6 or 7.

(4) A corporation under Oregon law is liable for punitive damages.

Subsequent to the decision in the case cited by appellant, *Pelton* v. *General Motors Acceptance Corporation,* 139 Or. 98, 7 P.2d 263, there has been another decision by the Supreme Court of Oregon relating to punitive damages assessed against a corporation, in which the whole subject of punitive damages is thoroughly discussed. In that case, *McCarthy* v. *General Electric Co. et al.,* 151 Or. 519, 49 P.2d 993, an award of punitive damages was sustained on appeal to the Supreme Court of the State of Oregon.

The attitude of the federal courts in this matter is well settled, as in the case of *General Motors Acceptance Corporation* v. *Froelich,* 273 F.2d 92, which in-

volved the repossession of an automobile. Actual damages of $150.00 and punitive damages of $2,500.00 were awarded to the plaintiff by the jury on the ground that such repossession was wrongful. In sustaining the award of punitive damages the court says, at p. 94:

> "While the evidence in the present case leaves some doubt as to the right of plaintiff to punitive damages within the principle thus established, we think the evidence did raise an issue for the jury in that regard. It is not essential in every case that an executive officer of high rank actively participate in the corporate conduct, as in Wardman-Justice. See Jackson v. General Motors Acceptance Corp., supra. A corporation such as defendant with offices in a number of cities and engaged in widespread activities, necessarily delegates authority to its agents to be used on its behalf. If these agents in the exercise of their delegated authority, acting through regular corporate channels, engage in conduct which, except for the corporate nature of their principal, makes out a case for punitive damages, the corporation is not shielded therefrom simply by the absence of explicit authorization or ratification of the particular conduct. A contrary rule would permit punitive damages against smaller concerns as in the Wardman-Justice case, but not against a large corporation whose size and ramifications make express authorization by the top executives of its working-level agents highly unlikely. The question is whether the wanton, reckless or malicious action of the agents or employees can fairly be said to be truly that of the principal."

Also, the United States Court of Appeals for the Ninth Circuit, this court, sustained an award for punitive damages in the case of *Pacific Telephone & Telegraph Co.* v. *White,* 104 F.2d 923. In reviewing a case on appeal from the U. S. District Court for the

District of Oregon, it upheld an award of $9,750.00 punitive damages by a jury against the appellant for the assault made on the appellee by one Hansley who was Chief Special Agent for the appellant. In an exhaustive opinion the court reviewed all of the cases decided by the Oregon Supreme Court concerning punitive damages assessed against corporate defendants, including *Pelton* v. *General Motors Acceptance Corp.*, 139 Or. 198, 7 P.2d 263, 9 P.2d 128, and *McCarthy v. General Electric Company,* 151 Or. 519, 49 P.2d 993. The court says at page 928:

> "It having been brought out in the testimony that Hansley was Chief Special Agent for the appellant company and not a menial servant, in the light of Lipman, Pelton and McCarthy cases, we are brought to the conclusion that the trial court correctly declined to give requested instructions III and VI and committed no error in its instructions given on the question of punitive damages."

These cases apparently hinge on the terminology 'menial servant'. Certainly Mr. Reklau was not what could be considered a menial servant, since he was a general agent, as admitted in all of the pleadings including the amended pretrial order (R. 13) and the company approved for the use of Mr. Reklau and furnished to him apparently Plaintiff's Exhibit 5, which was the foundation for the perpetration of the fraud practiced. If anything, Mr. Reklau was less a menial servant and more the alter ego of the defendant appellant, than was the case in either *Pelton* v. *General Motors, supra, McCarthy* v. *General Motors, supra,* and the *Pacific Telephone & Telegraph* case decided by this court.

The case cited by the appellant, *Union Deposit Co.* v. *Moseley* (Texas Civ. App), 75 S.W.2d 190, and the rule there applied has no application in Oregon in accordance with the finding of the Ninth Circuit as laid down in *Pacific Telephone & Telegraph Co.* v. *White, supra.*

It might also be noted at this point that Texas has laid down what is probably the most severe rule of any state with relation to the assessment of punitive damages against a corporation, and certainly is on the minority side of the courts in its views, which are not followed in this jurisdiction. There is ample precedent in both the Oregon law and the decisions of the federal court, including the Court of Appeals for the Ninth Circuit, to support the findings of the United States District Court for the District of Oregon in relation to punitive damages.

(5) Since the plaintiff was proceeding in an action at law he is not required to act with the speed demanded in a rescission under an equity theory.

(6) In an action for damages on a tort theory, the return of dividends is not required.

(7) The plaintiff in order to waive any of his rights must act with full knowledge of not only his rights but what he is waiving, and he had neither the knowledge of his rights and by his action has not waived his right to bring an action for damages.

(8) Plaintiff did not attempt to rescind and was not required to act promptly.

In responding to the above four points, which are treated together by the appellant, the appellee again stresses the fact that these four points all deal and treat with the subject of rescission, which has previously been discussed under point (1) and point (2). Rescission was not the remedy sought, nor was it the theory of the trial of the case.

The case of *Massachusetts Bonding and Insurance Co.* v. *Anderegg et al.*, 83 F.2d 622 (9th Cir., 1936), was a case in which the insurance company, appellant, after learning of the facts upon which it predicated its refusal to pay on its policy, accepted additional premiums, and the court there held that it had waived any right ot insist on the provisions of the policy, which led it to refuse to pay claims; in effect, a type of estoppel.

The case of *Browning* v. *Rodman,* 268 Pa. 575, 111 A. 877, has no application here.

Farrington v. *Granite State Fire Insurance Company of Portsmouth,* 120 Ut. 109, 232 P.2d 754, is authority for the principle that a general agent of an insurance company can waive certain known requirements with respect to fire insurance, and the court there held that the general agent had waived those requirements and the company was thus bound.

Sheppard v. *Blitz, supra,* has been discussed at length previously.

The trial court in this case discussed the matter of waiver (R. 20, 142) and properly rejected the claim of the appellant that the appellee had waived his right to

sue for damages for fraud. The trial court, in its opinion (R. 19, 20), discussed the matter of waiver at some considerable length, and that matter was before the court. It is true that the actions of the appellee were such as would have precluded his right to rescission, but his actions did not bar his right to bring an action for damages.

Selman v. *Shirley,* 1938, 161 Or. 582, 85 P.2d 384.

(9) The plaintiff did rely upon the representations of the agents of the appellant in entering into the insurance contract.

The fact that Dr. Lee made some investigation of the company to determine their financial status does not in any way controvert the fact that he relied on the statements of the agents in entering into this transaction. He so testified (R. 50). The assertion by the appellant in his brief at p. 39, that the claims of the agents as alleged by Dr. Lee may yet come true is not in any way determinative of the issues in this case. The policy of insurance was not as represented to Dr. Lee. The court held, and properly so, that the representations were fraudulent and were made wilfully.

"V

> "The representations made by the salesmen and general agent were material, false, and known by them to be false, and were made knowingly and wilfully. In making such representations the salesmen and general agent acted as agents of the company and within the scope of their employment."
> (Findings of Fact V, R. 22)

CONCLUSION

It is respectfully submitted:

First: That the United States District Court for the District of Oregon had jurisdiction over the parties and subject matter herein involved.

Second: That the representatives as alleged in plaintiff's complaint and amended pretrial order were abundantly established by the evidence presented and that actionable fraud was amply shown.

Third: That Dr. Lee waived none of his rights by any of his actions:

Fourth: The record and the evidence amply support the award of damages to the appellee.

Fifth: The award of punitive damages is justified in the light of decisions of the Oregon courts, the United States District Court for the District of Oregon and other federal courts including the United States Circuit Court of Appeals for the Ninth Circuit.

Respectfully submitted,

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